

Service Date: August 25, 1994

DEPARTMENT OF PUBLIC SERVICE REGULATION  
BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MONTANA

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|                                     |                   |
|-------------------------------------|-------------------|
| IN THE MATTER of the Application )  |                   |
| of the La Casa Grande Water )       | UTILITY DIVISION  |
| Company for Authority to Increase ) |                   |
| Rates and Charges for Water )       | DOCKET NO. 91.2.3 |
| Water Service to its East Helena, ) |                   |
| Montana Customers. )                | ORDER NO. 5610d   |

FINAL ORDER

APPEARANCES

FOR THE APPLICANT:

Robert Cummins, Attorney at Law, 1 Last Chance Gulch,  
Helena, Montana 59601.

FOR THE INTERVENORS:

Mary Wright, Staff Attorney, Montana Consumer Counsel, 34  
West 6th Avenue, Helena, Montana 59620.

Jerome Woodward, Water Subscriber, P.O. Box 533, East  
Helena, Montana 59635.

FOR THE COMMISSION:

Martin Jacobson, Staff Attorney, 1701 Prospect Avenue,  
Helena, Montana 59620.

Ron Woods, Rate Analyst, 1701 Prospect Avenue, Helena,  
Montana.

BEFORE:

BOB ANDERSON, Chairman  
DAVE FISHER, Commissioner  
BOB ROWE, Commissioner

BACKGROUND

1. On January 17, 1992, LWC petitioned for interim rate relief in Docket No. 91.2.3 and filed an affidavit in support of its petition. In the affidavit LWC itemized costs totalling \$8,754 claimed for capital maintenance to the system. Further, the Applicant indicated that it would borrow \$9,000 at 13 percent interest, with a repayment period of 36 months. LWC requested an annual revenue increase of approximately \$3,640 to service the three year \$9,000 debt obligation.

2. On February 24, 1992, the Commission having considered the merits of the Applicant's January 17th interim request, issued Order No. 5610 authorizing the Applicant interim rate relief. Order No. 5610 authorized the Applicant to amortize \$9,000 in loan proceeds obtained from a financial institution. As a condition for interim relief the Order provided that implementation of the interim rates obligated LWC to conduct an engineering assessment of the water system. If LWC failed to complete the engineering assessment after implementing the rates, the Commission stated it would revoke the interim increase. LWC

never implemented the increased rates authorized in Order No. 5610.

3. On August 4, 1992 LaCasa Grande Estates Water Company (Applicant or LWC) filed an amended application with the Montana Public Service Commission (Commission) for authority to increase water rates and charges to its East Helena, Montana customers on a permanent basis by approximately 37.2 percent for a revenue increase of approximately \$10,800. Concurrently LWC filed an application for an interim increase in rates for 100 percent of the proposed permanent increase.

4. LWC filed the amended interim and permanent rate increase application on August 4, 1992, in lieu of the application filed on January 17, 1992. LWC requested authorization of rates to service a proposed loan totalling \$27,000, to be retired over a three year period. The Applicant stated that the proceeds from the loan would be used to pay for water system improvements completed in 1991 costing approximately \$10,200 and to pay for an engineering assessment costing approximately \$17,000.

5. On August 26, 1992, the Commission issued Order No. 5610a authorizing interim rate relief to amortize \$27,000 in loan proceeds used to fund capital improvements and pay for an

engineering assessment.

6. On February 24, 1993, LWC filed a Motion to Amend its rate increase petition filed August 4, 1992. LWC requested approval of a monthly increase in rates of \$8.75 to recover increased operation and maintenance expenses and a \$3.33 monthly increase per customer for a period of three years to finance replacement of three pumps.

7. LWC's February 24, 1993, amended rate increase application, if granted in its entirety, would generate approximately \$32,544 in additional annual revenue from an average rate increase of approximately 110 percent.

8. On July 7, 1993, the Commission held a properly noticed public hearing in the Commission offices on the application for rate increase. For the convenience of the public an evening session was held July 7, 1993 at the same location.

#### FINDINGS OF FACT

9. At the public hearing the Applicant presented the testimony and Exhibits of:

Robert Cummins, Secretary/Treasurer, LWC  
James E. Taylor, Consulting Engineer

The MCC presented the expert testimony of Mark Smith from

the Montana Department of Health and Environmental Sciences. Ten public witnesses testified. Jerome Woodward intervened on his on behalf and presented himself as a witness.

10. The rate increase proposal has three components: 1) a permanent increase in the monthly base rate of \$8.75 to recover projected operation and maintenance expenses; 2) a temporary increase of \$6.00/month to cover the cost of a loan obtained to pay the costs associated with an engineering assessment and 1991 capital improvements; and 3) a temporary increase of \$3.33/month to cover the cost of an anticipated loan for capital improvements to the water system. The components of LWC's proposed rate increase will be discussed under separate headings.

11. The MCC argued as it did successfully in Docket 90.1.4, Order No. 5527, that the Commission should deny any rate relief to LWC on the grounds that the company was providing inadequate service to its customers. LWC countered that during periods of peak demand on the system, which is when customers experience service problems, it is operating the existing facilities at or beyond the design capacities of the facility. LWC opined that since it was operating the system at design capacity approved by the Montana Department of Health and Environmental Sciences it was providing reasonably adequate service under the

circumstances.

12. For purposes of this order the Commission accepts LWC's representation that the existing system is operating at approved design capacity and, therefore, is providing reasonably adequate service. The Commission, however, cautions LWC that if recommended improvements contained in the engineering evaluation are not undertaken to alleviate the peak demand service problems the issue of adequacy of service will be revisited.

Engineering Assessment/Loan Repayment

13. LWC is requesting that the Commission authorize rates to service an executed loan totalling \$27,000, to be retired over a three year period (scheduled to be retired September, 1995). The proceeds from the loan were used to pay for water system improvements completed in 1991 costing approximately \$10,200, and to pay for an engineering assessment costing approximately \$17,000.

14. The Montana Department of Health and Environmental Sciences (DHES) obtained an order from the State District Court in Cause No. CDV-90-444 which directed LWC to complete an engineering assessment for its water utility operation. In Order Nos. 5527 and 5610 the Commission stated that it supported LWC hiring an engineer to conduct an engineering assessment of the

water system because consumers had been experiencing service problems for an extended period of time. LWC is obligated, under the terms of the court order, to complete an engineering assessment that identifies existing facility deficiencies and contains recommended improvements for correcting these deficiencies.

15. LWC engaged the services of J.E. Taylor and Associates (Taylor) to conduct the water system evaluation. Taylor completed and submitted an interim Water System Evaluation to the Company in January, 1993. This report identified two primary reasons for low pressure on the LWC system: 1) the large quantities of water demanded and 2) the inability of the system to deliver these quantities. The report identified seven possible capital improvement scenarios that could potentially rectify the inadequate pressure problems being experienced on the system.

16. During 1991 LWC undertook a capital maintenance program which included the replacing a 5 horse power pump, pump testing of two wells, installing a 25 horse power pump, as well as several minor electrical and plumbing improvements. The total cost for the 1991 capital maintenance as supported by affidavit was approximately \$10,200.

17. The Commission is satisfied with its findings in Order No. 5610 regarding the recovery of debt costs associated with 1991 improvements and will not repeat those findings.

18. LWC has executed a loan with its shareholders in the amount of \$27,000, to be repaid over a three year period, to cover the costs of the engineering assessment and the 1991 improvements. The Commission finds that the Applicant's proposal to increase rates by \$6.00 per month to make the monthly payment of \$896.88, through September, 1995 is reasonable.

#### Anticipated Capital Improvements

19. LWC's consultant, Taylor stated "System capacity can be increased from about 300 gpm to 400 gpm by replacing existing pumps in Wells 1, 2, and 3 with more efficient and higher volume pumps, provided the aquifer continues to produce as it did during the pump test...The cost of the pumps and pump tests would be approximately \$5,000 per well. Because the pumps in the first three wells are nearly worn out, they will require replacement very soon...." (page 16, Water System Evaluation). Taylor further stated "[T]he first improvements made to the water system will, by necessity, be the replacement of the pumps in wells 1, 2, and 3. The existing pumps will not carry the load of another irrigation season. Upgrading the capacity of the pumps will help



increase system capacity somewhat, however, immediate actions should be take to reduce the quantity of water needed. Water conservation measures... should be initiated and encouraged...." Id. p.21.

20. Taylor's Water System Evaluation forms the basis for LWC's request for a \$3.33 monthly rate increase for a period of 3 years for anticipated system improvements. LWC requests a rate increase to recover costs associated with a \$15,000 loan having a term of 3 years and a maximum interest rate of 12%.

21. Although LWC is a privately-owned public utility, it is requesting regulatory treatment on a cost basis similar that afforded municipal utilities under this Commission's jurisdiction. The Applicant has not proposed in this filing, and does not intended in the future, to establish a rate base.

22. The Commission evaluates the need for increased rates to private utilities through analysis of rate base, operating revenues and expenses, capital structure and rate of return. The Commission has developed this practice over many years and embraces all privately owned public utilities under its jurisdiction. In Order No. 5610a the Commission deviated from general ratemaking policy for this private utility to ensure continued service to LWC's subscribers and because persistent

service complaints, along with the court order, convinced the Commission funding of an engineering evaluation to identify system deficiencies was necessary. LWC once again asks the Commission to deviate from general ratemaking policy. This request warrants examination of the prudence of continuing special ratemaking treatment for this utility.

23. In the regulatory arena privately-owned utilities are expected to attract the capital (debt and equity) necessary to obtain capital items essential for the operation of the utility.

Once the capital items become "used and useful" in utility operations, the capital investment is returned to the utility through depreciation expense over the life of the asset. LWC's requested ratemaking treatment achieves the same result as described above except that the value of the asset is not returned over the useful life of the asset but rather the term of the debt instrument.

24. The Commission is concerned about LWC's continuing request to allow recovery of capital costs over the term of a debt instrument as opposed to the useful life of the assets. Many utility assets have useful lives of 20 to 50 years. Allowing capital recovery based on contract terms of 3 to 7 years, as opposed to useful life, will result in

intergenerational rate inequities.

25. In the instant application the contract term and useful life may be approximately the same, thus presenting no apparent rate inequity. However, it is not good regulatory policy to deviate routinely from ratemaking policies developed over many years. These policies are intended to balance the interests of the ratepayer and the utility. If contract term, as opposed to useful life, consistently dictated capital recovery the current subscriber would be disadvantaged. Using contract term to establish the capital recovery period front-end loads the cost on to the current subscriber, providing a free ride to future subscribers, which is not good ratemaking policy. Utility rates should provide for recovery of costs imposed on the system by subscribers during the same period they receive the service.

26. Based on the preceding findings the Commission finds the Applicant's proposal to increase rates for recovery of debt costs associated with potential capital improvements should be denied.

#### Discussion

Within the next two years LWC will be required to make long-lived capital improvements to the system which it intends to finance with short-term debt. LWC intends to request, prior to

commencement of construction, capital recovery over the term of the contract as opposed to the life of the assets. This proposal will be unacceptable to the Commission.

If LWC intends to stay in the water utility business, it should start discharging its obligations in a manner consistent with the duties and responsibilities imposed by law on it and other privately-owned public utilities. First, it should recognize that the utility has the obligation to establish a rate base on which it is entitled to earn a return. The utility also has the responsibility to attract the capital necessary for construction of new or replacement facilities. The Commission does not have a duty to raise capital for the utility or act as the utility's guarantor.

The Commission previously discussed the public utility financial obligation with LWC in an order on rate relief:

...As a privately-owned public utility, it is the responsibility of the utility to obtain funding either through equity investment or issuance of debt to fund capital improvements. After the capital expenditures have been made and are used and useful, the Commission will allow the utility depreciation expense and a return on investment. The Commission finds the Applicant's request for funding of \$18,100 in capital improvements is inappropriate, and therefore denies the request. The Commission would recommend that the Applicant start establishing a rate base through the proposed capital improvements. Order No. 4898, Dated May 20, 1982, Finding of Fact No. 8.

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Every utility in this state should recognize that it cannot be permitted to let its facilities threaten the health, welfare or safety of its consumers. Utility's that enjoy monopolistic privileges must bear the burden of providing reasonably adequate service and facilities. No utility should be heard to argue, such as the Applicant did in this Docket, that it cannot and/or will not make the necessary improvements because it does not have the financial resources. If the current management and/or owners of LWC are unable or unwilling to discharge their obligations in the operation of the public utility then they should arrange for some other entity to conduct those services. Order No. 5527, Finding of Fact 17, Dated December 18, 1990.

The Commission has not changed its position on the duties

and obligations of a utility. If LWC is not financially viable because it cannot attract capital to construct facilities necessary to provide reasonably adequate service or meet environmental mandates, then the owners, with customer participation, should examine alternative forms of ownership. These alternative forms of ownership include formation of a water users' association or establishment of a county water district.

Operation and Maintenance Expenses

27. LWC indicated that on a cash basis it was incurring actual monthly expenses of \$2,062 for annual operating costs of \$24,744. On a proforma basis LWC indicates that its monthly operating expenses are \$3,734 for an annual cost of \$44,808.

28. Consumers testifying at the hearing indicated that their major concerns regarding proforma operating expenses were the salary costs charged to the LWC operation and the provision for payment of legal fees. Consumers were concerned at the lack of significant evidence substantiating the hours devoted by each of the employees, on a part-time basis, to the utility operation.

The consumers also expressed serious dissatisfaction with the performance of LWC in the area of customer service.

29. The proforma operating statement reveals that \$1,786 of the \$3,734 monthly proforma expense claimed by LWC are salary and

salary-related costs. The 1992 and proforma financial statements reflect the following monthly salary levels for employees (excluding fringe benefits):

|                          | <u>1992</u> | <u>Proforma</u> |
|--------------------------|-------------|-----------------|
| Project Operator         | \$ 400      | \$ 475          |
| Business/Project Manager | -0-         | 600             |
| Sec/Bookkeeper           | 550         | 580             |

Assuming, as the Company has, that there are 150 subscribers, the salary component of the proposed monthly bill is \$11.03 per customer. On a cash basis the salary component of the current bill, which excludes any payment for the Business/Project manager, is \$6.33 (\$550 sec/bookkeeper + \$400 Project Operator - 150). The large proportion of the salary component in the monthly bill and the consumer testimony concerning management and customer service calls for examination of the proposed salary levels.

30. Various public witnesses testified about customer service problems, such as LWC's failure to return phone calls, abusive or indifferent treatment during contacts, blame shifting during service complaints, and failure to respond to complaints or service inquiries. The testimony indicated that lack of interest in customer service was endemic.

31. Each position for which LWC is requesting compensation

is directly involved in customer service. A public utility sells both its commodity and service. Consumers by and large measure service provided by a utility by the quality of customer service they receive. This Commission cannot recognize increased pay levels for customer service employees when public testimony demonstrates that LWC is not providing prompt, courteous and effective customer service. The Commission finds that the Applicant's request to recover increased labor expenses for the project operator and secretary should be denied.

32. Although denying the request for increased wages the Commission must address the issue of compensation for the business/project manager. Throughout this proceeding the Applicant relied on Commission determinations in a 1982 LWC rate order (Order No. 4898) to support compensation of \$600 per month for this position. In 1982 it was reasonable for this Commission to authorize that level of compensation for the position; today it is not.

33. This business/project/ manager is in charge of managing and overseeing all aspects of LWC's operations. Therefore, it is the responsibility of the manager to ensure that all utility obligations are discharged. Customers of LWC demonstrated that the customer service function of the company is woefully



inadequate and unresponsive. It would be imprudent to reward the position with the full compensation requested when customer service is deficient. The Commission finds it appropriate to adjust the compensation amount to be recovered in rates and to allow compensation of \$400 per month, the same as for the system operator.

34. LWC has proposed inclusion of \$100 per month in the cost of service to cover legal costs. LWC indicated that the legal fees included in the cost of service were required for defense of the Department of Health and Environmental Sciences (DHES) lawsuit against LWC. Consumers expressed reservations about LWC's proposal to recover costs associated with its defense of the DHES lawsuit. The consumers indicated they received no benefit from LWC's defense against this action and should not be required to reimburse the company for the costs incurred.

35. The Commission shares the consumers concerns regarding customer benefit derived from LWC's defense of the DHES lawsuit.

In its post hearing brief LWC stated the following as the cause of the DHES litigation:

LCW has been in a legal battle with the Department of Health and Environmental Sciences since July 1990, hereinafter referred to as DHES, over the requirement of the application of the Ten States standards

for operation of the system and the requirement to have obtained prior approval for the resetting of well number one in 1988 and for a request that LCW conduct an engineering study to evaluate the operability of the system versus the design approved by DHES in 1977. LCW resisted the requirement for the study as proposed as being too costly and that it would require the expenditure of approximately \$25,000.00...

LWC's reasons for litigating with DHES appear to validate the concerns regarding consumer benefit from the litigation. It appears that DHES is attempting to force LWC to comply with reasonable operating standards and to ascertain, through a study, any operational or design inadequacies that exist on the system.

It should not require litigation to force management of a water utility to comply with reasonable standards of operation. The Commission finds that LWC's request to include \$100.00 per month in its cost of service for legal fees should be denied.

36. LWC has requested that it be allowed to include in its monthly cost of service \$300.00 for repair and maintenance. The record indicates that this amount is not unreasonable. The Commission will, however, impose a requirement on this funding. The \$300.00 monthly allowance should be placed in an earmarked account for repair and maintenance with all disbursements from the account being separately accounted for and documented on the

books and records of LWC.

37. Based on the preceding the Commission finds LWC's total monthly operating expenses to be \$3,305.14. The Commission finds that the total annual operating expenses of the utility is \$39,661.68.

38. The total monthly costs of operating LWC are \$4,202.02 (See Findings of Fact Nos. 18 and 37) for a total annual operating cost of \$50,424.24.

#### Rate Design

38. LWC has requested that the Commission authorize a flat rate and metered rate schedule for its operations. In anticipation of fully metering its system, LWC has requested approval of a metered rate schedule. The Commission denies LWC's request for approval of a metered rate schedule in this proceeding because the Commission has insufficient information upon which to develop a metered rate schedule for LWC.

39. In the Water System Evaluation Mr. Taylor indicates that metering the water system would be the least cost improvement for rectifying the pressure problems currently experienced by consumers. Mr. Taylor stated metering the system could easily reduce water consumption by 25 to 30 percent and provide a fair means of charging subscribers. The Commission

agrees with Mr. Taylor's reasons for fully metering the system.

40. The Commission finds that LWC should prepare a meter installation plan. Metering all connections will promote rate equity, provide a conservation incentive, promote efficient resource management and delay any potential need to expand plant capacities. Within 120 days of this order LWC shall submit to the Commission a metering plan which includes economic analysis showing that the costs do not exceed the benefits; a proposed installation schedule not to exceed three years; and a statement indicating that it has consulted with LWC subscribers to discuss the metering program.

41. Once LWC has completed metering one-third its water system, it may apply to the Commission for a metered rate. Upon receiving the application, the Commission will approve a metered rate on an interim basis, subject to refund of amounts collected in excess of LWC's authorized revenue requirement.

42. LWC shall continue to assess a monthly flat rate to all of its residential consumers. The Commission finds the monthly flat rate to be assessed should be \$28.01 through September, 1995 and \$22.01 thereafter.

#### CONCLUSIONS OF LAW

1. The Applicant, La Casa Grande Water Company, is a public utility as defined in Section 69-3-101, MCA. The Montana Public Service Commission properly exercises jurisdiction over the Applicant's rates and service pursuant to Section 69-3-102, MCA.

2. The Commission has provided adequate notice and an opportunity to heard as required by Section 69-3-303, MCA, and Title 2, Chapter 4, MCA.

3. The rates and rate structure approved in this Order are just and reasonable. Sections 69-3-201, and 69-3-330, MCA.

#### ORDER

THEREFORE THE MONTANA PUBLIC SERVICE COMMISSION ORDERS THAT:

1. LaCasa Grande Estates Water Company shall file rate schedules designed to generate total annual revenues of \$50,424.24 through September, 1995, for its East Helena, Montana service area. On October 1, 1995 LaCasa Grande Estates Water Company shall file rates designed to generate total annual revenues of \$39,661.68. The revenues shall be generated by increasing rates and charges to all customer classifications as provided herein.

2. This rate increase is in lieu of and not in addition to the rate increase approved in Order No. 5610a.

3. The rates approved herein shall not become effective until approved by the Commission.

4. LaCasa Grande Water Company shall within 120 days of the service date of this order submit the meter installation plan provided for herein.

DONE IN OPEN SESSION THIS 22nd day of August, 1994 by a vote of 3-0 at Helena, Montana.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

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BOB ANDERSON, Chairman

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BOB ROWE, Vice Chairman

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DAVE FISHER, Commissioner

ATTEST:

Ann Purcell  
Acting Commission Secretary

(SEAL)

NOTE: Any interested party may request that the Commission reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.